



Proposed Act

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An Act

To facilitate check truncation, to foster innovation in the check collection system without mandating receipt of checks in electronic form, and to improve the overall efficiency of the nation's payments system.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE; PURPOSES.

(a) SHORT TITLE.--This Act may be cited as the "Check Truncation Act".

(b) PURPOSES.--The purposes of this Act are to facilitate check truncation, to foster innovation in the check collection system without mandating receipt of checks in electronic form, and to improve the overall efficiency of the nation's payments system.

SEC. 2. DEFINITIONS.

For purposes of this Act--

(1) ACCOUNT.--The term "account" means a deposit account with a bank.

(2) BANK.--The term "bank" means--

(A) any person, located in a State, engaged in the business of banking;

(B) a Federal Reserve Bank;

(C) a Federal Home Loan Bank; and

(D) to the extent it acts as a payor, the U.S. Treasury, the U.S. Postal Service, or a State or local government.

(3) BANKING DAY.--The term "banking day" has the meaning given to such term in section 229.2 of title 12, Code of Federal Regulations.

(4) BUSINESS DAY.--The term "business day" has the meaning given to such term in section 229.2 of title 12, Code of Federal Regulations.

(5) CHECK.--The term "check" means a draft, payable on demand and drawn on or payable through or at an office of a bank, whether negotiable or not, that is handled for forward collection or return, including a substitute check. Such term does not include a noncash item or an item payable in a medium other than United States money.

(6) CONSUMER.--The term "consumer" means an individual who--

(A) with respect to a check handled for forward collection, draws the check on an account used primarily for personal, family, or household purposes; or

(B) with respect to a check handled for return, deposits the check into or cashes the check against an account used primarily for personal, family, or household purposes.

(7) INDEMNIFYING BANK.--The term "indemnifying bank" means a bank that provides an indemnity under section 5.

(8) MICR LINE.--The term "MICR line" (or "magnetic ink character recognition" line) means the numbers, which may include the bank routing number, account number, check number, check amount, and other information printed near the bottom of a check in magnetic ink in accordance with generally applicable industry standards.

(9) NONCASH ITEM.--The term "noncash item" has the meaning given to such term in section 229.2 of title 12, Code of Federal Regulations.

(10) PERSON.--The term "person" means a natural person, corporation, unincorporated company, partnership, government unit or instrumentality, trust, or any other entity or organization.

(11) RECONVERTING BANK.--The term "reconverting bank" means the bank that creates a substitute check. If a substitute check is created by a party other than a bank, then the reconverting bank is the first bank that transfers or presents that substitute check.

(12) RETURNING BANK.--The term "returning bank" has the meaning given to such term in section 229.2 of title 12, Code of Federal Regulations.

(13) SUBSTITUTE CHECK.--The term "substitute check" means a paper reproduction of the original check that--

(A) contains an image of the front and back of the original check;

(B) bears a MICR line containing all information required under generally applicable industry standards for substitute checks;

(C) conforms, in paper stock, dimension, and otherwise, with generally applicable industry standards for substitute checks; and

(D) is suitable for automated processing in the same manner as the original check.

(14) STATE.--The term "state" means a State of the United States, the District of Columbia, Puerto Rico, the U.S. Virgin Islands, or a territory, possession, or dependency of the United States.

(15) TREASURY CHECK.--The term "Treasury check" means a check drawn on the United States Treasury.

(16) TRUNCATE.--The term "truncate" means to remove an original paper check from the check collection or return process and in its place to send to a recipient a substitute check or, by agreement, information relating to the original check (including but not limited to data taken from the MICR line of the original check or an electronic image of the original check), whether with or without subsequent delivery of the original paper check.

(17) UNIFORM COMMERCIAL CODE.--The term "Uniform Commercial Code" or "U.C.C." means the Uniform Commercial Code in effect in a State.

(18) Unless the context requires otherwise, the terms not defined in this section have the meanings set forth in the U.C.C.

SEC. 3. GENERAL PROVISIONS GOVERNING SUBSTITUTE CHECKS.

(a) NO AGREEMENT REQUIRED.--A person may deposit, present, or send for collection or return a substitute check without an agreement with the recipient, so long as a bank has made the warranties in section 4 with respect to that substitute check.

(b) LEGAL EQUIVALENCE.--A substitute check is the legal equivalent of the original check for all purposes, including Federal and state law, and for all persons if it--

(1) accurately represents all of the information on the front and back of the original check as of the time the original check was truncated; and

(2) bears the legend: "This is a legal copy of your check. You can use it the same way you would use the original check."

(c) **INDORSEMENTS.**--A reconverting bank shall ensure that the substitute check that it creates bears all indorsements applied by parties that previously handled the check (whether in electronic form or in the form of the original paper check or a substitute check) for forward collection or return.

(d) **IDENTIFICATION OF RECONVERTING BANK.**--A reconverting bank shall identify itself as a reconverting bank on the substitute check that it creates so as to preserve any previous reconverting bank identifications in conformance with generally applicable industry standards.

(e) **APPLICABLE LAW.**--A substitute check that is the legal equivalent of the original check under subsection (b) shall be subject to all other applicable Federal or state law as if it were the original check, to the extent such law is not inconsistent with this Act.

SEC. 4. WARRANTIES.

(a) **SUBSTITUTE CHECK WARRANTIES.**--A bank that transfers, presents, or returns a substitute check and receives consideration for it warrants to the transferee, any subsequent collecting or returning bank, the depository bank, the drawee, the drawer, the payee, the depositor, and any indorser (regardless of whether the warrantee receives the substitute check or another paper or electronic form of the substitute or original check) that--

(1) the substitute check meets all the requirements for legal equivalence under section 3(b); and

(2) no depository bank, drawee, drawer, or indorser will receive presentment or return of the substitute check, the original check, or a copy or other paper or electronic version of the substitute check or original check such that it will be asked to make a payment based on a check it has already paid.

(b) **TRUNCATED TREASURY CHECK WARRANTIES.**--Any bank that truncates a Treasury check and receives consideration for it warrants to the transferee, any subsequent collecting or returning bank, the depository bank, the drawee, the drawer, the payee, the depositor, and any indorser (regardless of whether the warrantee receives another paper or electronic form of the original Treasury check) that it has forwarded the original Treasury check for safekeeping in accordance with section 13.

SEC. 5. INDEMNITY.

(a) **INDEMNITY.**--A reconverting bank that creates a substitute check, and each bank that subsequently transfers, presents, or returns that substitute check in any electronic or paper form, and receives consideration for such transfer, presentment, or return shall indemnify the transferee, any subsequent collecting or returning bank, the depository bank, the drawee, the drawer, the payee, the depositor, and any indorser, up to the amount described in subsections (b) and (c), to the extent of any loss incurred by a recipient of a substitute check, if that loss is due to the receipt of a substitute check instead of the original check.

(b) **INDEMNITY AMOUNT.**--The amount of the indemnity under subsection (a) shall be the amount of any loss (including costs and reasonable attorney's fees and other expenses of representation) proximately caused by a breach of a warranty provided under section 4 if that loss would not have occurred had the original check been transferred or presented. In the absence of a breach of a warranty provided under section 4, the amount of the indemnity shall be the amount of any loss, up to the amount of the substitute check plus interest and expenses (including costs and reasonable attorney's fees and other expenses of representation), if that loss would not have occurred had the original check been transferred or presented.

(c) **COMPARATIVE NEGLIGENCE.**--If a loss described in subsection (a) results in whole or in part from the negligence or failure to act in good faith on the part of an

indemnified party, then that party's indemnification under this section shall be reduced in proportion to the amount of negligence or bad faith attributable to that party.

(d) **EFFECT OF PRODUCING ORIGINAL CHECK.**--If the indemnifying bank produces the original check, it is liable only for losses covered by the indemnity that are incurred up to the time the original check is provided to the indemnified party, and the indemnifying bank has a right to a return of any funds it has paid under the indemnity in excess of those losses. Production of the original check does not absolve the indemnifying bank from any liability on a warranty that it has given under this Act or other law.

(e) **SUBROGATION OF RIGHTS.**--A bank that indemnifies a party under this section may attempt to recover from another party based on a warranty or other claim. Each indemnifying bank is subrogated to the rights of any indemnified party to the extent of the indemnity. Each indemnified party has a duty to comply with all reasonable requests for assistance from the indemnifying bank in connection with any claim related to the check that the indemnifying bank brings against a warrantor or other party.

SEC. 6. EXPEDITED RECREDIT PROCEDURES FOR CONSUMERS.

(a) **WHEN A CONSUMER MAY MAKE A CLAIM.**--

(1) A consumer may make a claim for expedited recredit from the bank that holds the consumer's account if the consumer asserts in good faith that--

(A) the bank charged the consumer's account for a substitute check that was provided to the consumer and that was not properly charged to that account or for which the consumer has a warranty claim;

(B) the consumer suffered a resulting loss; and

(C) production of the original check is necessary to determine the validity of the charge to the consumer's account or the warranty claim.

(2) The consumer shall submit the claim to the bank within 60 calendar days after the relevant statement or substitute check is made available to the consumer, whichever is later. If the consumer's ability to submit the claim within the 60-calendar-day time period is delayed due to extenuating circumstances, including, but not limited to, extended travel or hospitalization, the 60-calendar-day period shall be extended by a reasonable amount of time.

(b) **HOW TO MAKE A CLAIM.**--

(1) To make a claim under subsection (a), the consumer shall provide to the bank that holds the consumer's account--

(A) a description of the claim, including an explanation of why the substitute check was not properly charged to the consumer's account or of the warranty claim;

(B) a statement that the consumer suffered a loss and an estimate of the amount of the loss;

(C) the reason why production of the original check is necessary to determine the validity of the charge to the consumer's account or the warranty claim; and

(D) sufficient information to identify the substitute check and to investigate the claim.

(2) The bank holding the consumer's account may, in its discretion, require the consumer's claim under this subsection to be in writing.

(c) **RECREDIT TO CONSUMER.**--If the consumer makes a claim in accordance with subsections (a) and (b) against the bank holding the consumer's account, then that bank shall either produce the original check and show that the substitute check was properly charged to the consumer's account or recredit the consumer's account for the amount of the claim, up to the amount of the substitute check or \$2,500, whichever is less, no later than the business

day following the banking day the consumer makes the claim. The bank shall credit the consumer's account for the remainder of the amount of the claim, up to the amount of the check, plus interest, on the business day following the banking day on which the bank determines that the consumer's claim is valid, but no later than 20 business days following the banking day the consumer makes the claim. Providing a recredit does not absolve the bank from liability for wrongful dishonor under the U.C.C. or other law or from liability for additional damages under section 5 or 8.

(d) AVAILABILITY OF RECREDIT.--

(1) Except as provided in paragraphs (2) and (3), a bank that provides a recredit to a consumer's account under subsection (c) shall make recredited funds available for withdrawal by the start of the next business day after the business day that the bank is required to recredit the consumer's account.

(2) A bank may delay availability of a recredit provided under paragraph (1) until the twentieth business day following the banking day on which the consumer makes such claim if--

(A) The claim is made during the 30-calendar-day period beginning on the banking day the consumer's account was established;

(B) Without regard to the charge that is the subject of the claim,

(i) on six or more banking days within the preceding six months the consumer's account balance was negative or would have become negative if checks or other charges to the account had been paid, or

(ii) on two or more banking days within the preceding six months the consumer's account balance was negative or would have become negative in the amount of \$5,000 or more if checks or other charges to the account had been paid; or

(C) The bank has reasonable cause to believe that the claim is fraudulent, based on facts (other than the fact that the check in question or the consumer is of a particular class) that would cause a well-grounded belief in the mind of a reasonable person that the claim is fraudulent.

(3) If there has been an interruption of communications, computer, or equipment facilities, or other emergency condition beyond the control of the bank, the bank may delay availability of a recredit until a reasonable period after the emergency has ceased, provided the bank exercises such diligence as the circumstances require.

(e) REVERSAL OF RECREDIT.--If a bank determines that a substitute check for which the bank recredited a consumer's account under subsection (c) was properly charged to the consumer's account, the bank may reverse the recredit to the consumer's account if, upon reversing the recredited amount, it:

(1) provides to the consumer the original check;

(2) notifies the consumer of the date and amount of the reversal; and

(3) notifies the consumer that the bank will honor checks or other payments to third parties (without charge to the consumer as a result of an overdraft) for five business days after the notification. The bank shall honor payments as specified in the notice, but need honor only payments that it would have paid if the recredit had not been reversed.

SEC. 7. EXPEDITED RECREDIT PROCEDURES FOR BANKS.

(a) WHEN A BANK MAY MAKE A CLAIM.--

(1) A bank may make a claim for expedited recredit from a previous indemnifying bank if--

(A) the claimant bank (or a bank it has indemnified) has received a

claim for expedited recredit from a consumer under section 6 or would have been subject to such a claim had the consumer's account been charged;

(B) the claimant bank has suffered a resulting loss or is obligated to recredit a consumer's account under section 6; and

(C) production of the original check is necessary to determine the validity of the charge to the consumer's account or the warranty claim.

(2) The claimant bank shall submit the claim to the indemnifying bank within 120 calendar days after the calendar day of the transaction that gave rise to the claim.

(b) HOW TO MAKE A CLAIM.--To make a claim under subsection (a), the claimant bank shall provide to the indemnifying bank--

(1) a description of the claim, including an explanation of why the substitute check cannot be properly charged to the consumer's account or of the warranty claim;

(2) a statement that it has suffered a loss or is obligated to recredit a consumer's account under section 6 and an estimate of the amount of the loss or recredit;

(3) the reason why production of the original check is necessary to determine the validity of the charge to the consumer's account or the warranty claim; and

(4) sufficient information for the indemnifying bank to identify the substitute check and to investigate the claim. This information may include, for example, a copy of the substitute check or checks at issue, but in that case the claimant bank shall take reasonable steps to ensure that any such copies are not mistaken for the legal equivalent of the check under section 3(b) nor sent or handled as forward collection or returned checks. At the request of the indemnifying bank, the claimant bank shall provide a copy of the consumer's written claim under section 6(b), if the claimant bank had obtained the consumer's claim in writing.

(c) RECREDIT BY INDEMNIFYING BANK.--No later than 10 business days after the business day it receives a claim under subsection (a), the indemnifying bank shall either provide to the claimant bank the original check or recredit the claimant bank for the amount of the claim, up to the amount of the substitute check, plus interest. Providing a recredit under this subsection does not absolve the indemnifying bank from liability for additional damages under section 5 or 8. If the indemnifying bank produces the original check to the claimant bank, its right to a return of any funds it has reccredited pursuant to this subsection is governed by section 5(d).

SEC. 8. MEASURE OF DAMAGES.

(a) MEASURE OF DAMAGES.--Except as provided in section 5, damages for breach of warranty or failure to meet any requirement of this Act shall be an amount equal to the loss suffered as a result of the breach or failure, but not more than the amount of the substitute check or checks in question, plus interest and expenses (including costs and reasonable attorney's fees and other expenses of representation) related to the substitute check. Damages, if any, are reduced by the amount, if any, that the claimant receives and retains as a recredit.

(b) COMPARATIVE NEGLIGENCE.--If a party incurs damages that resulted in whole or in part from that party's negligence or failure to act in good faith, then the damages due to that party under subsection (a) shall be reduced in proportion to the amount of negligence or bad faith attributable to that party.

SEC. 9. STATUTE OF LIMITATIONS AND NOTICE OF CLAIM.

(a) STATUTE OF LIMITATIONS.--An action to enforce a claim under this Act may be brought in any United States district court, or in any other court of competent

jurisdiction, and shall be brought within one year after the cause of action accrues.

(b) NOTICE OF CLAIM.--Except as provided in subsection (c), unless a person gives notice of a claim to the indemnifying or warranting bank within 30 days after the person has reason to know of the claim and the identity of the indemnifying or warranting bank, the indemnifying or warranting bank is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(c) NOTICE OF CLAIM BY CONSUMER.--A timely claim by a consumer under section 6 for expedited recredit also constitutes timely notice of a claim by the consumer under subsection (b).

SEC. 10. EFFECT ON OTHER LAW.

This Act shall supersede any provision of Federal or State law, including the Uniform Commercial Code, that is inconsistent with this Act, but only to the extent of the inconsistency.

SEC. 11. VARIATION BY AGREEMENT.

The provisions of section 7 may be varied by agreement, but no other provisions of this Act may be varied by agreement.

SEC. 12. REGULATIONS.

(a) BOARD OF GOVERNORS.--The Board of Governors of the Federal Reserve System may by regulation clarify or otherwise implement the provisions of this Act or may modify the requirements imposed by this Act to further the purposes of this Act, including but not limited to reducing risk, accommodating technological or other developments, and alleviating undue compliance burdens.

(b) TREASURY.--The Secretary of the Treasury may by regulation clarify or otherwise implement the provisions of this Act or may modify the requirements imposed by this Act with respect to Treasury checks to further the purposes of this Act, including but not limited to reducing risk, accommodating technological or other developments, and alleviating undue compliance burdens.

SEC. 13. TRUNCATION OF TREASURY CHECKS.

(a) SAFEKEEPING OF ORIGINAL TREASURY CHECKS.--Any bank that truncates a Treasury check shall, promptly after truncation of the original Treasury check, send the original Treasury check for safekeeping to a Federal Reserve Bank.

(b) NOT TO BE SENT FOR FORWARD COLLECTION.--An original Treasury check sent for safekeeping under subsection (a) shall be sent in a manner that reasonably ensures that such original Treasury check will not be handled as a forward collection item.

SEC. 14. EFFECTIVE DATE.

(a) Except as provided in subsection (b), this Act shall become effective on July 1, 2003, or one year after the date of enactment, whichever is later.

(b) With respect to Treasury checks, the Secretary of the Treasury may extend the effective date of this Act.

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